

STATE OF IOWA  
DEPARTMENT OF COMMERCE  
UTILITIES BOARD

IN RE:  INTERSTATE POWER COMPANY	DOCKET NOS. EEP-94-40 TF-99-178 TF-99-179 (ECR-96-1)
--	---

**FINAL DECISION AND ORDER**

(Issued June 28, 2000)

**I. PROCEDURAL HISTORY**

On June 14, 1999, Interstate Power Company (Interstate) filed with the Utilities Board (Board) an application to modify its energy efficiency plan. Interstate proposed to reduce its energy efficiency budget by \$1,853,322, which represents a 20 percent spending reduction for electric programs and a 30 percent reduction for gas programs. Because the proposed modification represented a significant spending reduction, the Board on July 14, 1999, docketed the proposed plan modification and at the same time scheduled a prudence review to evaluate the reasonableness and prudence of Interstate's implementation of its approved plan. Iowa Code § 476.6(19)"e" (1999).

In addition to the Consumer Advocate Division of the Department of Justice (Consumer Advocate), the Iowa Industrial Intervenors (III) and Ag Processing Inc (Ag Processing) intervened in the proceeding. Interstate, Consumer Advocate, and III filed prefiled testimony. A hearing on the modification and prudence review was

subsequently scheduled for April 11, 2000. All parties were represented at the hearing and post-hearing briefs were filed.

## **II. DISCUSSION**

### **A. OVERVIEW**

Energy efficiency costs are recovered by a utility through an automatic adjustment mechanism over a period not to exceed the term of the plan. Iowa Code § 476.6(19)"e". This section also addresses review of those expenditures and provides, in relevant part:

The board shall periodically conduct a contested case proceeding to evaluate the reasonableness and prudence of the utility's implementation of an approved energy efficiency plan and budget. If a utility is not taking all reasonable actions to cost-effectively implement an approved energy efficiency plan, the board shall not allow the utility to recover from customers costs in excess of those costs that would be incurred under reasonable and prudent implementation and shall not allow the utility to recover future costs at a level other than that what the board determines to be reasonable and prudent. If the result of a contested case proceeding is a judgement against the utility, that utility's future level of cost recovery shall be reduced by an amount by which the programs were found to be imprudently conducted.

The burden is on the utility to prove it has taken all reasonable actions to cost-effectively implement its approved plan. 199 IAC 35.13.

The prudence review for Interstate is for calendar years 1996, 1997, and 1998. There are two issues. First, whether Interstate was prudent in the implementation of its energy efficiency plan during those years. Second, if Interstate is found to be imprudent, whether some of the costs incurred in the implementation of its energy

efficiency plan should be disallowed. The Board will address the prudence issues first. It is difficult to make a decision regarding a significant plan modification without first evaluating how Interstate has implemented its approved plan.

The review of Interstate's proposed plan modification is governed by Iowa Code § 476.6(19)"c" and 199 IAC 35.6(4). The Board has the authority to accept, reject, or modify any proposed plan modification.

As a preliminary matter, the Board will address the arguments raised by the industrial intervenors, Ill and Ag Processing. Their arguments focused on justifications for phasing out energy efficiency that is supported by a utility's ratepayers. Such arguments are misplaced. The General Assembly has mandated that electric and gas public utilities, and particularly rate-regulated electric and gas utilities, provide energy efficiency programs. Iowa Code § 476.6(17). Specific provisions are provided for implementation, cost review, and cost recovery. Iowa Code § 476.6(19). The Board, and utilities, have a duty to carry out this legislative mandate for energy efficiency in a manner that provides the most benefits for Iowa's citizens.

## **B. PRUDENCY**

The Board's review is for calendar years 1996, 1997, and 1998. The evidence presented by Interstate demonstrates that, except for the electric interruptible program discussed below, Interstate was prudent in implementing its approved energy efficiency plan in 1996 and 1997. In fact, Interstate's performance in 1996 could be called exemplary.

Interstate's success in 1996 and 1997 make 1998 all the more puzzling. While Interstate's natural gas programs continued to be successful, Interstate's electric programs fell far short of meeting their projected energy and capacity savings. The Board concludes that with respect to 1998 electric programs, Interstate was imprudent and did not take all reasonable actions to cost-effectively implement its approved energy efficiency plan. Interstate reduced its promotion budget in 1998 by 95 percent and program results suffered. Interstate made no showing on the record as to why promotions were limited, other than to state that it was due to an impending name change as a result of a merger. However, there was no showing promotion budgets in areas other than energy efficiency were so drastically reduced. Interstate did claim some programs were saturated with participants, but there were no studies or other evidence to show market saturation. In fact, it appears likely results would have dramatically improved if the promotion budget had not been significantly reduced.

There may be an explanation why promotions were suspended, but it was not offered by Interstate on the record. For example, it may be prudent to reduce the promotion for certain programs if the monitoring and evaluation results show that increased rebates are more effective than advertising or direct customer contact. Interstate offered no evidence on any substitutes for the lack of promotion. Interstate's failure to produce convincing evidence to explain its lack of promotion and perceived market saturation results in the conclusion that Interstate has not satisfied its burden. 199 IAC 35.13.

Interstate claimed that because its programs showed benefits under various benefit/cost ratios and because its overall spending was adequate, there could be no imprudence. The Board does not believe, however, that benefit/cost ratio results are the definitive standard in a prudence review. These ratios are a derivation of broader performance measures that form the basis for evaluating an energy efficiency plan and do not have a direct relationship to the net benefits of a plan in terms of capacity and energy savings. Overall spending is not an adequate measure because it does not indicate that the monies were used effectively.

More than benefit/cost ratios or overall spending, prudence must be determined by evaluating a plan in terms of the primary goals of energy efficiency programs, which are to reduce demand for both capacity and energy, thereby delaying or deferring expensive generation plant construction and reducing ongoing energy costs. These savings benefit consumers, industry, and the utility. Interstate's 1998 performance demonstrates that significant potential capacity and energy savings for electric programs were not realized. Interstate must be held accountable for its performance. In contrast, Interstate's natural gas programs met or exceeded the established goals for both capacity and energy savings.

The Board also concludes that Interstate was imprudent in implementing its electric interruptible program for the years 1996 and 1997. There were no participants in 1996 or 1997, but Interstate did not suspend spending for the program until 1998. A prudent utility in its monitoring and evaluation efforts would have looked at the 1996 results and tried something different, whether it was redesigning the program, increasing advertising, or dropping the program. To stay with the status

quo and continue to expend money on a program with no participants is not prudent. The results of this program are particularly disappointing because a successful program would have provided Interstate with critical peak capacity savings.

**C. DISALLOWANCE**

Iowa Code § 476.6(19)"e" mandates that "[i]f a utility is not taking all reasonable actions to cost-effectively implement an approved energy efficiency plan, the board shall not allow the utility to recover from customers costs in excess of those costs that would be incurred under reasonable and prudent implementation . . ." (emphasis added). Once a finding of imprudence is made, the Board has no option but to disallow recovery of costs in excess of those that would have been incurred under reasonable and prudent implementation. The prior statutory scheme of rewards and penalties has been repealed. Under that system, rewards could be granted for exemplary performance in some areas and penalties imposed for poor performance in others.

The current statutory standard is difficult to apply, particularly in this case. The statute appears largely designed for situations where a utility spends more money than is warranted on energy efficiency. In Interstate's case, total spending is not the issue, but spending in certain categories is. The most glaring figures are the reduction in the 1998 promotion budget and the increase in 1998 program management costs. It is difficult to understand why program management costs were increasing each year while total energy efficiency spending decreased. With the drastic reduction in the promotion budget, reductions in program management costs would also generally be expected. While Interstate argued some of the program

management costs were related to programs requiring direct customer contact, this does not explain the magnitude of the increase.

The Board believes Interstate's decision to reduce the promotions budget made it a foregone conclusion that some of the energy efficiency programs would not succeed or reach their potential. In attempting to determine an appropriate disallowance, several methods could be used. For example, the Board could assume that the program management costs should be reduced by the same percentage as the reduction in the advertising budget. Even if costs associated with direct customer contact were allowed, leaving only those management costs for programs that require promotion for support, this method would result in a disallowance of \$499,479. (Consumer Advocate Sch. D, p. 1). Another option would be to disallow costs based on the percentage of the electric capacity and/or energy goals met. These methods result in disallowances from approximately \$275,000 to \$450,000. (Interstate 1/14/00 filing, Part A).

While basing disallowances on the percentage of the capacity and/or energy goals met links the disallowances to results, the Board will not use this method here. Actual results cannot be taken alone to determine prudence. Programs can fail or not reach their potential for a variety of reasons, not all of which are caused by unreasonable or imprudent implementation.

Because no satisfactory alternative was presented at hearing, the Board will determine the amount of the disallowance by looking at the percentage of the total energy efficiency plan budget used for electric program management costs in 1996, a year the Board found that Interstate was generally prudent in implementing its energy

efficiency plan. That year, 9.2 percent of the total budget was spent on electric program management costs. If 9.2 percent of the total budget had been spent on electric program management in 1998, \$397,006 would be the amount. Instead, \$647,825 was spent. Therefore, the total disallowance of the electric program management budget is the difference between these two figures, or \$250,819. While the Board may not use this method in future proceedings, it is reasonable based on the evidence, or lack thereof, presented here.

In addition to the electric program management budget, all costs for the interruptible program in 1996 and 1997, or \$30,830, will be disallowed. Interstate was imprudent in failing to discontinue or redesign the program in 1997 after there were no participants in 1996 and monitoring reports throughout 1996 and 1997 showed the program was failing. Spending for the program was finally suspended in 1998. Adding the two disallowances, the total disallowance is \$281,649.

#### **D. PLAN MODIFICATION**

The Board cannot accept Interstate's proposed plan modification. Because of the lack of commitment to energy efficiency in 1998, as evidenced by the promotion budget, the Board does not know how successful the existing plan can be. The only way to find out is to implement Interstate's currently approved plan.

The evidence does not support Interstate's allegations regarding market saturation. If market saturation is a problem, it was not established in this case. In addition, as discussed earlier, high benefit/cost ratios and overall spending levels are not necessarily indicative of overall prudence. The level of spending reduction



proposed by Interstate is simply not supported by the evidence presented to the Board in this proceeding.

The Board wants to encourage Interstate to become an active participant in energy efficiency with input from the Board's staff, Consumer Advocate, and other parties. Therefore, the Board will require Interstate to meet quarterly on an informal basis with Board staff, Consumer Advocate, and other interested parties to this proceeding to review progress in implementing Interstate's plan and in remedying deficiencies in 1998 plan implementation. This way, the Board hopes any problem areas can be caught early in the process and remedial action taken promptly.

At this time, the Board intends to commence another prudence review, for calendar years 1999 and 2000, on or before July 1, 2001. In the next review proceeding, Interstate will be required to address or provide the following items:

1. An explanation of Interstate's efforts to identify and analyze market barriers to adoption of energy efficiency technology and operating methods.
2. An explanation of Interstate's efforts to use all reasonable methods to overcome identified market barriers.
3. An explanation of any innovative methods and newly available technologies incorporated into Interstate's programs.
4. A detailed narrative of Interstate's actions to implement programs and the responses of customers, trade allies, and others to the program implementation.
5. Detailed data and analysis showing program impacts for 1999 and 2000, in both hard copy and electronic form.

The Board is hopeful that with a redoubled effort and the broad guidelines provided by the Board, Interstate will be able to replicate its energy efficiency successes in 1996 and 1997.

### **III. FINDINGS OF FACT**

1. It is reasonable to conclude that Interstate was not taking all reasonable actions in 1998 to prudently implement the electric side of its approved energy efficiency plan.
2. It is reasonable to conclude that Interstate was not taking all reasonable actions in 1996 and 1997 to prudently implement its interruptible program.
3. It is reasonable to disallow cost recovery of \$250,819 in electric program management costs for 1998 and \$30,830 in costs for the 1996 and 1997 interruptible program, for a total cost disallowance of \$281,649.
4. It is reasonable to deny Interstate's request for plan modification.

### **IV. CONCLUSIONS OF LAW**

The Board has jurisdiction of the parties and the subject matter in this proceeding, pursuant to Iowa Code chapter 476 (1999).

### **ORDERING CLAUSES**

#### **IT IS THEREFORE ORDERED:**

1. Interstate Power Company is ordered to refund to customers through the adjustment clause the amount of energy efficiency costs, \$281,649, found by the Board to have been imprudently incurred, and shall file a reconciliation for the

Board's consideration to reflect the disallowance within 30 days from the date of this order.

2. The request for plan modification filed by Interstate Power Company on June 14, 1999, is denied, and Interstate is directed to implement its energy efficiency plan approved on January 18, 1996, and as modified by Board orders issued on May 22, 1998, and January 5, 1999.

3. Tariff filings TF-99-178 and TF-99-179 are rejected.

4. Interstate shall arrange the quarterly meetings provided for in this order, with the first meeting to be held as soon as practical after the date of this order.

5. In Interstate's next prudence review filing, which shall be made on or before July 1, 2001, Interstate shall provide the information identified in this order.

6. Motions and objections not previously granted or sustained are denied or overruled. Any argument in the briefs not specifically addressed in this order is rejected either as not supported by the evidence or as not being of sufficient persuasiveness to warrant comments.

**UTILITIES BOARD**

/s/ Susan J. Frye

/s/ Diane Munns

### **DISSENT**

While I agree with parts of my colleagues' decision and analysis, I must respectfully dissent from the decision to impose cost disallowances at this time. I would not make a final finding of imprudence now. Instead, I would suspend any disallowance pending the Board's prudence review in 2001. If at that time Interstate has lived up to the specific performance standards in the original plan, provided the information and analysis required in the discussion found in the majority decision regarding plan modification, and actively participated in the quarterly meetings, I would not find the costs disallowed by the majority to be imprudently incurred.

My decision is driven by several factors. First, the record in this proceeding is, in my view, inadequate for a comprehensive prudence review. While I recognize Interstate has the burden of establishing prudence, this is the first energy efficiency prudence review conducted by the Board where a disallowance is imposed. The standards set forth in this decision were not known at the time Interstate filed its testimony and exhibits and the hearing was held.

Second, I believe that incentives generally work better than regulatory mandates in achieving results. Interstate performed well in 1996 and 1997, and there is no reason Interstate cannot once again reach that level of performance. Rather than simply mandating that Interstate perform at these levels, I believe better results will be obtained by offering an incentive for Interstate to put forth its best efforts in improving plan performance.

Third, this result is not prohibited by Iowa Code § 476.6(19)"e." As noted by the majority, the statute was apparently not drafted to address the facts presented

here, where overall plan spending is adequate but spending in specific categories is either too high or too low. More importantly, what is prudent at one point in time is not always prudent at a subsequent point in time. For example, if the prudence review had been only for calendar year 1996, that year's spending for the interruptible program would likely have been found to be prudent. Calendar year 1996's spending arguably became imprudent in a prudence review covering 1996 through 1998 because Interstate continued the spending in 1997 without taking corrective action. Likewise, I view the spending in 1998 to be imprudent only if Interstate fails to take the subsequent corrective action outlined by the Board.

Given the inadequate record and the lack of established review standards, I am willing to provide Interstate an opportunity to revitalize its energy efficiency programs. Energy efficiency is designed to provide energy and capacity savings that will benefit both utilities and their customers. If Interstate lives up to the guidelines set forth in the order, I believe that when the Board conducts a second prudence review in 2001, calendar year 1998 costs will be seen as part of the framework for successful programs in 2000 and beyond. The best way to ensure this is to provide Interstate an incentive to return to its past successes.

/s/ Allan T. Thoms

ATTEST:

/s/ Raymond K. Vawter, Jr.  
Executive Secretary

Dated at Des Moines, Iowa, this 28<sup>th</sup> day of June, 2000.